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Problems and Prospects of Contract Farming in India

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Abstract

In view of the farmers' movement against the three Acts dealing with agriculture passed by the Parliament ,contract farming has come into the limelight. In this context it would be useful to discuss such issues as: what is contract farming, what are the features of contract farming, what are the benefits of contract farming to the parties involved in contract farming, what are the problems of contract farming etc. The present paper discusses these issues in the most simple manner.

Keywords: Different types of farming, Contract farming, Contacting company, Legal framework, Regulation of contract farming, Measures for the promotion of contract farming.

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Introduction

Now-a-days the term 'contract farming' is frequently heard. The Mckinsey report submitted to the erstwhile Left Front Government of West Bengal recommended introduction of contract farming. Following this recommendation the Left Front Government of West Bengal considered the proposal seriously. The Government of India's National Agricultural Policy (2000) stated, "Private sector participation will be promoted through contract farming and land leasing arrangements to allow accelerated technology transfer, capital inflow and assured market for crop production, especially of oil seeds, cotton and horticultural crops". Recently contract farming has come into limelight in view of farmers' protests against the three Acts passed by the Parliament. In this context it would be useful to discuss such issues as : what is contract farming, what are the features of contract farming, what are the benefits of contract farming etc. The purpose of this paper is to discuss these issues in the most simple manner.

Different Types of Farming:

We have heard about different types of farming such as peasant farming. tenant farming, capitalist farming, collective farming, cooperative farming etc. A new addition to this list is contract farming. Before taking up contract farming let us have a brief discussion on the features of different types of farming

In the case of peasant farming the owner of land cultivates his land himself. This type of farming is mostly found in India. In this type of farming cultivation is done by the family members jointly. A few agricultural labourers from outside the family may be engaged but most of the labour is given by the members of the family. Vital decisions like what crops to be produced or how much amount of land to be used to produce any crop are taken by the members of the family.

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During the plan period in India the stated objective of the Government of India was to promote the system of peasant farming based on small size of holdings. It was for this reason that a ceiling was imposed on family land holding and surplus land above the ceiling was taken over by the Government and distributed among the rural landless agricultural labourers.

Instead of cultivating his own land a land owner can lease out his land to others in lieu of rent payable in cash or in kind. This type of farming is known as tenant farming or share-cropping. Along with peasant farming tenant farming is also present in West Bengal and India. Several laws have been enacted in India to protect the interests of the tenants who are also known as *bargadars*. The Government of West Bengal had taken up a programme of Operation Barga to record the names of bargadars so that bargadars cannot be evicted at will.

In peasant farming or tenant farming the size of the holding is small. But if the size of the holding is not large, economies of large scale production cannot be enjoyed . Good Irrigation system cannot be developed on small holdings. Improved technology and farm mechanization cannot also be adopted on small holdings. Hence, to increase farm productivity large farming is needed. Two models of large farming have been used in many countries. One is the model of capitalist farming and the other is the model of socialist collective farming Capitalist farming is present in advanced capitalist countries like the US.A., U.K. etc. Here one individual is the owner of a large farm. He engages hired labourers in lieu of wages. The land owner is also the owner of agricultural implements The workers get wages. They do not get any share of the product produced by them. Capitalist farms are, so to say, factories in the field.

On the other hand, socialist collective farming system was prevalent in the erstwhile Soviet Union. In this model a collective farm society is formed by the members who join the farm. The society becomes the owner of lands of the members. The members work in the collective farm. The land is cultivated jointly. The members get share of the produce in proportion to the labour contributed by them. The collective farm system does not permit private ownership in land. After the disintegration of Soviet Union and fall of socialism in east European countries collective farms are also disintegrating. Socialist countries like China, Vietnam and Cuba are also introducing reforms in the agricultural sector to permit private ownership in land.

Another way of getting the benefits of large scale production while retaining private ownership in land is the introduction of cooperative farming. In this farming system cultivators join voluntarily. Lands of different cultivators are pooled together for the purpose of cultivation, though individual ownership is retained. Cattle and other agricultural implements are also pooled together for joint cultivation. Each member gets wage in proportion to the labour hours contributed and share of the produce in proportion to the amount of land contributed. Though attempts were made to introduce this type of cooperative farming in India, there was not much progress.

Features of Contract Farming

After considering different types of farming let us now turn to contract farming. Contract farming is introduced in the case of peasant farming where the peasants cultivate their own land. There are two parties in any contract farming. One party is the landowner or peasant who cultivates his own land. The other party is a contracting company who purchases agricultural products from the landowners. According to the contract, the farmer is required to plant the contractor's crop on his land, and to harvest and deliver to the contractor a quantum of produce, based upon anticipated yield and contracted acreage. This could be at a pre-agreed price. Towards these ends, the contractor supplies the farmer with selected inputs, including the required technical advice. Thus under contract farming the contractor supplies all the inputs required for cultivation while the farmer supplies land and labour. However, the terms and nature of the contract differ from case to case.

The Government of India Runs the largest Contract Farming Model

In one sense the Government of India has worked as the largest contractor engaged in contract farming during the period of Green Revolution. Like a contracting company the Govt. of India supplied inputs like HYV seeds, new technology, water for irrigation, fertilizers, insecticides, pesticides, subsidized credit etc. Again the Govt. purchased agricultural crops through agencies like the FCI at predetermined procurement prices. The new agricultural strategy adopted by the Govt. of India was a resounding success. As a result of the Green Revolution food security was assured. Import of food grains under P.L480 agreement was stopped. Farm incomes increased. Public distribution system was safeguarded. More employment was created in the agricultural sector.

Success however came at a cost. : Agriculture today is not diversified. There is overemphasis on cereals and sugarcane. There is low or no focus on pulses and oilseeds. Moreover, in the Green Revolution the role of the government was most important. There was only a marginal role for the private sector. Essential Commodities Act became a means of ensuring government procurement.

Minimum support price announced by the Government was a benchmark reference pricing, rather than a farmer safety net. Green Revolution has also created environmental problems for the rural economy. To improve productivity there has been excessive use of fertilizers, insecticides and pesticides. There has also been excessive water usage leading to soil degradation. Singular focus on supported crops has destroyed crop-diversity. Productivity of land is also decreasing due to continuous cultivation of the same crops. To succeed in this context contract farming needs to go well beyond its simple definition.

Why Contract Farming

Farming is an age-old means of livelihood for millions of Indians. However, there have been few systems/models in which farmers are assured of a market for their produce, leave alone a remunerative price. Farmers have on occasion had to throw their produce away for want of buyers. This is one side of the coin.

On the other side is the agro-based and food industry which requires timely and adequate inputs of good quality agricultural produce. This underlying paradox of the Indian agricultural scenario has given birth to the concept of contract farming which promises to provide a proper linkage between the farm and the industry.

Apart from this there are several reasons for the introduction of contract farming in India. Some of the reasons can be mentioned as follows:

1. Financial burden of central and state governments will be reduced. Private investment in agriculture will increase. This is required in the context of liberalization and privatization.
2. Contract farming is needed to bring about a market focus in terms of crop selection by Indian farmers.
3. Contract farming will generate a steady source of income at the individual farmer level;
4. Contract farming will provide a linkage between agriculture and processing industries. These will promote processing of agro-products and consequent value addition.
5. Contract farming will generate gainful employment in rural areas, particularly for landless agricultural labour. It will also reduce, as far as possible, any seasonality associated with such employment.
6. Contract farming will reduce migration of labour from rural areas to urban areas. It will promote rural self-reliance in general by pooling locally available resources and expertise to meet new challenges.

As a matter of fact contract farming will be mutually advantageous. Both the farmers and the contracting company will benefit as a result of contract farming. Let us first consider the advantages of contract farming to the farmers.

Advantages to the Farmers

The farmers adopting contract farming will get the following advantages: 1. The farmers will be exposed to world class mechanized agro-technology. This will increase productivity; 2. The farmers obtain an assured price for their products. They also get market outlet for their products; 3. The farmers get healthy disease-free nursery, agricultural implements and improved technology from the contracting company, 4. There will be crop monitoring on a regular basis. Technical advice will be provided free of cost at the doorstep of the farmer. This will help the farmer to get assured output.

Advantages to the Company

The contracting company will also get some advantages. These advantages are mentioned below:

1. The company will get uninterrupted and regular flow of raw materials for its processing plant; 2. The company will get protection from fluctuation in market pricing as the company enters into forward contract with the farmers; 3. It will be possible for the company to formulate long term planning. If the move is successful for one crop it can be extended to other crops. As a result the company can diversify its product base and farmers can also produce several products; 4. The company gets a dedicated supplier base. The contract farming builds long term commitment between the company and the farmers. It also generates goodwill for the organization.

A Few Successful Cases

Before considering the problems of contract farming we shall first mention a few examples of successful contract farming in India.

(i) Contract farming in wheat is being practised in Madhya Pradesh by Hindustan Lever Limited (HLL), Rallis, and ICICI. Under the system, Rallis supplies agri-inputs and know-how, and ICICI supplies finance. HLL, the processing company, which requires the farm produce as raw material for its food processing industry, provides the buyback arrangement for the farm output. In this arrangement farmers benefit through the assured market for their produce in addition to timely, adequate and quality input supply including free technical know-how; HLL benefits through supply chain efficiency; while Rallis and ICICI benefit through assured clientele for their products and services.

(ii) Another successful case of contract farming is the case of Pepsi Foods Limited which set up a state-of-the-art tomato processing plant at Zahura in Hoshiarpur district of Punjab. The company intended to produce aseptically packed pastes and purees for the international market. However, before long, the company recognized that investment in agro processing plant would not be viable unless the yields and quality of agricultural produce to be processed were up to the international standard. The company entered into strategic partnership with Punjab Agricultural University and Punjab Agro Industries Corporation. Pepsi company followed the contract farming method described earlier where the grower plants the company's crops on his land, and the company provides selected inputs like seeds, agricultural practices and regular inspection of the crop and advisory services on crop management. Encouraged by the sweeping success of contract farming in tomato in several districts of Punjab, Pepsico has been successfully emulating the model in food grains (Basmati Rice), spices (chillies) and oilseeds (groundnut) as well, apart from other vegetable crop like potato.

(iii) Appachi Cotton Company (ACC) of Coimbatore district of Tamil Nadu hit the headlines in May 2002 for the street play it employed to encourage farmers to sow cotton seeds in their fields. The Appachi formula ensured that its farmer members never went short of money and materials during the crucial 100 days of crop cycle. The contract assured the farmers easy availability of quality seeds, farm finance at an interest rate of 12% p.a., door delivery of fertilizers and pesticides at discounted rates, expert advice and field supervision every alternate week and a unique selling option through a MOU with ACC. The core principle lies in the formation of self-help groups by farmers. Each farmer belonging to an SHG is sanctioned Rs. 8000/- per acre as crop loan @12% p.a. interest. All the participating farmers are asked to issue post-dated cheques for loan they avail. No prior price fixing is done in this model. ACC has only the first right to purchase at the market price. The Appachi formula of contract farming has been so successful that Tamil Nadu Government is now keenly interested in replicating this formula in various cotton growing districts of the state.

Problems of Contract Farming

We can mention some of the problems in the way of introduction of contract farming in India. In the first place there is no credible enforcement mechanism for contract farming in India. If any party involved in the contract does not honour the terms of contract there is no provision of giving any punishment to the offender. Secondly, since the size of the holdings is small the company will have to enter into contract with a large number of farmers. This increases costs of the company. Thirdly, there is lack of comprehensive crop insurance scheme in India. Hence the farmers cannot protect themselves against the risk of crop failure.

Even in the absence of a legal framework the company can take certain measures to make the contract farming system effective. For example, the company can maintain a proper database on farmers and can avoid repeat defaulters in future contracts. The company can publicize the names of defaulters in the locality of default. The social stigma then usually suffices as a disincentiveto default. The company can also introduce a system of incentives, rewards and public recognition for those who can fulfill their targets. This will maintain a high motivation level among the farmers. The farmers can be encouraged to set their own targets. They can also be permitted to sell their surplus output in the open market after meeting their contractual obligation to the company.

What measures can the government take?

In order to promote contract farming the government can take several measures. Some of these suggestedmeasures can now be stated. In the *first place*, state level legislation should be made for the regulation of contract farming. The government should declare that purchase interference by a third party in a contract farming programme would be regarded as a cognizable offence. A quasi-judicial system of contract enforcement should be set up with the help of appropriate legislation. *Secondly,* the government should allow contract farming organizations to take out realistic and deregulated crop insurance policies. *Thirdly,* the government should give tax concessions or tax holidays to the companies engaged in contract farming. The government should also abolish taxes or duties on import of agri-equipment to be used in a registered contract farming programme. *Fourthly,* the government should instruct the ICAR and the University system to provide region specific crop solutions and make them part of public information domain. *Fifthly,* the government should facilitate import of new improved varieties of seeds / saplings / hybrids and technology for contract farmers / contracting companies.

Conclusion

The idea of contract farming is nothing new. During the British period contract farming was introduced in Bengal for the production of indigo. The farmers were forced to cultivate indigo by the processors who were known as *Nilkar Sahibs.* The sahibs had the patronage of the government. The exploitation of the indigo planters brought about revolt among the peasants. But present contract farming is not exploitative in nature. It is mutually advantageous. Moreover, the peasants enter into contracts with the company out of their own will. There is no compulsion on any peasant. Any farmer can leave the system just by not renewing the contract for the next period. It should, however, be noted that financially the company is stronger than individual farmers. Hence the terms and conditions of the contract may go against the interests of the farmers. Herein the government will have to come forward. The government will have to protect the interests of farmers through suitable legislations. The contract farming will be able to make important contribution to the growth of the agricultural sector in India. Given the diverse agro climatic zones, India can be a competitive producer of a large number of crops. What is needed is to convert our factor price advantage into sustainable competitive advantage. Contract farming offers one possible solution for this.

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